ALP ENERGY REVIEW

October 2013

Addressing Contradictions in the Nigerian Energy Landscape in 2013.
By Dr Dayo Ayoade PHD (Energy law and econs.), Senior Lecturer Petroleum, Electricity and Trade Law, University of Lagos.

Gathering gains and growing challenges – A fresh insight into the Indigenous Oil and Gas Market.
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Electricity Restructuring in Canada and the Role of its Bulk Trader: Potential Lessons for Nigeria?
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Evaluation of the Power Sector the transaction and Financial Advisor's Perspective.
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ALP Energy Review is a journal compiled and published by **Akindelano Legal Practitioners.** It is published in conjunction with the ALP Seminar Series

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Foreword (Oil & Gas Sector) by Dr. Layi Fatona

There is a wind of change afoot within the Nigerian Energy Sector. It is in uncharted territory. Never before in the history of the Sector has there been so much to play for especially as regards the participation of indigenous players in the multiple IOC assets divestment exercises.

Might we be looking at a situation soon when the majority of Nigeria's daily Oil production is by Nigeria is indigenous Oil and Gas companies?

Perhaps there's considerable time before that happens, however with the systematic auctioning of marginal fields, divestment by the IOCs and favourable local content Legislation, it is a time of unprecedented opportunities for indigenous Oil companies and we are likely to look back at this period as a major milestone in the development of the Nigerian Petroleum industry. It is a major sign of the times that Nigerian companies are beginning to eye both the Upstream and the Downstream sectors of the industry. There remain challenges of course which must be carefully approached if the industry is to be the success the nation has long hoped for.

Simultaneously the Power Sector also is showing a similar shift in paradigm. Through the privatisation Process, gone at last is the ubiquitous and Infamous PHCN but replaced by who? And how will they fare, given that the assets they have taken over are the self-same assets that NEPA and PCHN failed miserably to manage effectively. This is without a doubt one of the biggest tests of maturity of the private sector (and the privatisation policy itself).

The articles contained in this excellent journal will begin to touch on many of these challenges and issues seen through the eyes of various professionals and stakeholders whose contributions have been garnered by ALP into this document. It will be useful for professionals and potential investors, fund managers within and beyond the Nigerian Energy industry.

Dr. Layi Fatona
MD/CEO Niger Delta Exploration and Production Plc

Comments by Olayode Delano (ALP)

ALP ENERGY REVIEW is a publication compiled and published by Akindelano Legal Practitioners.

It presents an overview of the Nigerian Energy Sector and contains a series of articles which examine the status of the sector, business challenges, best practices legal issues and pragmatic solutions.

It is presented from the perspective of corporate participants, within the industry and contains articles from local players like UBA Investment and ALP as well as International firms with an interest in the Nigerian energy sector like Aird and Berlis (Canada), Rystad (Norway) and Dentons (UK).

This journal is useful to executives and decision makers in the Oil and Gas and Power sector, Banking and Finance, Investment companies Fund and managers and the entire spectrum of the corporate sector and create an insight for would-be investors, local and international.

The journal will be distributed to a segmented corporate database. It will also be available for download on our website **www.akindelano.com**. If you wish to have a copy please email us at Alp@akindelano.com 01 -9504742 or 016290918.

The publication is made in conjunction with the **ALP SEMINAR SERIES** which is scheduled for February of 2014.
The Theme of the Seminar is **THE NIGERIAN POWER SECTOR: WHAT NEXT AFTER PRIVATISATION.**

Olayode Delano
Partner ALP

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ADDRESSING CONTRADITIONS IN THE NIGERIAN ENERGY LANDSCAPE IN 2013

Dayo Ayoade Ph.D (Energy law and econs.), Senior Lecturer Petroleum, Electricity and Trade Law, University of Lagos.

The Nigerian energy landscape in 2013 has seemingly been plagued by a combination of long and short term issues that have not been resolved.

It manifests in a complex interaction of domestic and transnational factors that provide a strong perception that the sector faces fundamental challenges without any concerted action on the part of stakeholders to address the contradictions.

The Petroleum Industry Bill (PIB) 2012 remains perhaps the biggest hurdle to oil and gas developments in Nigeria.

In light of the stalled legal and policy framework, and highly disputed tax regime, exploration and production has declined steadily.

The reform process remains incomplete as the enactment of the bill should have completed the work of the Oil and Gas Sector Reform Implementation Committee (OGIC) inaugurated on 24th April 2000.

Apart from its 13 year journey, the PIB is unique for having at least 5 major incarnations before the extant 2012 version. That said, it boasts a detailed fundamental objectives section that have not traditionally featured in Nigerian legislation.

For example, the avowed intention behind the PIB to interalia – create a robust economic environment to attract investment; liberalise and deregulate the downstream petroleum industry; ensure transparency and good governance; create a commercially oriented national oil champion; and sustain Nigerian content capacity are not controversial, but the achievement of these objectives has not matched the rhetoric.

Another long term concern is the capacity of domestic banking and finance sector markets to fund energy projects.

Despite important improvements, big ticket transactions are still beyond the capacity of the Nigerian finance industry.

According to news reports, most of the current divestment transactions have been funded from outside the country ensuring a systemic loss to the Nigerian banking sector.

This is due essentially to the short term focus of the financial sector and its limited capacity to fund medium to long term gestation periods, necessary for deepwater oil field projects.

Apart from large projects, marginal field operators have also struggled to acquire financial support. The laudable marginal

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[1] According to Mark Ward, Chairman of OPTS and Managing Director, Mobil Producing Nigeria Unlimited, if the PIB is passed in its current form, upstream oil and gas will decline from 63% to about 25%. See PIB: FG, Oil Majors Disagreements Deepen, Vanguard newspaper 27th August 2013.

[2] Nigerian Banks Unable to Fund Large Oil, Gas Deals – Shell, http://www.vanguardngr.com/2013/05/nigerian-banks-unable-to- fund-large-oil-gas-deals-shell/#sthash.8bFXOF20.dpuf

fields policy originated under the Federal Government's 1991 Indigenous Concession Programme (later formalized in the 1996 Petroleum (Amendment) Act).

It allows indigenous oil companies enter into oil fields held by International Oil Companies (IOCs) which do not contain significant deposits and have not been developed for a considerable number of years due to field economics, technical difficulty etc Although the policy seemed promising yet after two decades, marginal fields account for only 2.1 % of crude oil production or 60,000 bpd.

In addition, only nine marginal fields are producing out of 24 marginal fields awarded in 2003 and five fields awarded under the discretionary powers of the President.

Active marginal field owners include Britania-U (Ajapa field); Frontier Oil (Uquo field); Midwestern Oil and Gas and Suntrust (Umusadege field); Platform Petroleum (Asuokpu/Umutu field); Pillar Oil (Obodogwa/Obodeti field); and Walter Smith and Morris Petroleum (Ibigwe field).

For the discretionary awards, Niger Delta Petroleum Development Company (Ogbelle field) and Oriental Energy (Okwok and Ebok fields) are involved in active production.

The limited success of marginal fields is also due to the harsh operating environment in Nigeria. There have been struggles with partnership arrangements imposed by the FG, technical/financial partnership issues, crude oil theft, pipeline vandalisation, host community problems, and inability of contractors to deliver projects on time.

Similarly, these operational difficulties have impacted significantly on IOC business, with Shell, Total, ENI, and Mobil declaring force majeure on crude oil exports in recent years.

Between 2011-2012, Shell and Total have divested assets in the Niger Delta reflecting the difficulty of doing business in the area. More upstream divestments have also been announced by diverse companies such as Chevron, Petrobras and ConocoPhillips, reflecting changes in internal business strategies.

In the LNG and natural gas sector, investment indecision and long lead times in implementing projects have exposed important new LNG projects to review, and possible cancellation.

The rise of Shale gas in North America and Europe has contributed to a sharp decline in gas prices and also raised investor concerns about project economics.

For example, the Final Investment Decision (FID) for Brass LNG initially planned for 2006 has still not been signed almost seven years later.

Similarly, Olokola LNG (OKLNG) FID has not been signed despite the fact that shareholders signed the Memorandum of Understanding in 2006. Also, the $12 billion FDI Train 7 of the Nigeria Liquefied Natural Gas (NLNG) project to increase production capacity from 22 to 30 million metric tons per year has been stalled since 2005. News reports now suggest that ConocoPhillips will divest its stake in Brass LNG, also putting pressure on NLNG

Train 7 in which it holds a 17% share. Furthermore, Shell and Chevron plan to divest their 53.25% stake in OKLNG.

Another important LNG issue has been the protracted tax dispute between a FG agency, the Nigerian Maritime Administration Safety Agency (NIMASA) and the NLNG. Failure by NLNG (49% owned by NNPC) to pay fiscal dues under the Nigerian Maritime Administration Act, LFN 2004, relying on an

[3] Ibid.

exemption from new taxes and dues under the Nigeria LNG (Fiscal Incentives, Guarantees and Assurances etc) Act LFN 2004 resulted in a physical blockage of exports by NIMASA. This resulted in NLNG having to declare force majeure on LNG exports.

It is hard to estimate the reputational risk damage that the nation has suffered from the incident. Though the matter is now settled, it seems to show a contradiction between the need to attract investment and protecting existing investment.

Next is the Nigerian Oil & Gas Industry Content Development Act (NOGICDA) 2010 which has sought to drive the development of domestic participation and indigenization of the energy industry. Though the NOGICD Act Schedule assigns local content values (above 60% mark) to construction and fabrication, procurement, marine operations and logistics among others, it is near impossible for these milestones to be achieved with the existing power and infrastructure deficit.

This is despite the Nigerian Content Development Fund (NCDF) that allocates one percent (1 %) of contract sum transactions to domestic companies for capacity development and expansion. It is difficult to judge whether the NCDF and 2006 ($350 million) Nigerian Content Support Fund (NCSF) have made meaningful contributions to Nigerian energy services businesses.

Unlike the PIB, the Electric Power Sector Reform (ESPR) Act 2005 provides a firm legal framework to address the challenges of the sector.

Key features of the ESPR Act include: creation of the Initial Holding Company (Power Holding Company of Nigeria) to assume assets, liabilities and employees of the National Electric Power Authority; unbundle PHCN into successor companies; electricity market development; establishment of the Nigeria Electricity Regulatory Commission (NERC); and privatization of succession companies.

These milestones have taken seven years to fulfill as the FG has had to address significant hurdles such as pension liabilities, high technical losses and vandalism.

More recently, the FG has sold the Transmission Company of Nigeria (TCN); 10 Distribution Companies (DISCOs) and 5 Generation Companies (GENCOs).

Despite these achievements, the nation continues to suffer poor electricity supply and this continues to undermine the energy business and industry development.

Hence it would seem that current investment patterns in Nigeria are unhealthy and perhaps damaging in the medium-long term.

Stagnation and divestment in energy cycle investments show a reinforcement of domestic problems such as failure to enactment the PIB and international competition from "unconventional" shale oil and gas discoveries, horizontal drilling and hydraulic fracturing.

Added to this is greater competition even from the African continent that has seen investment capital shift from proven Nigerian arena to East Africa (Kenya, Tanzania and Uganda) and Mozambican natural gas.

Undoubtedly, there is a need for the FG to actively intervene in the major crisis that cuts across the upstream oil and gas and LNG sectors.

While the downstream petroleum and natural gas sectors were not discussed above, it is pertinent to point out that these sectors are similarly stagnant with little head way in achieving deregulation (subsidy removal) and achieving the Gas Master Plan (GMP).

[4] See http://www.vanguardngr.com/2013/07/investment-indecision-stalls-lng-projects/#sthash.yHN39khD.dpuf

GATHERING GAINS AND GROWING CHALLENGES

A FRESH INSIGHT INTO THE INDIGENOUS OIL AND GAS MARKET

by Bimbola Kolawole

Since affirming its membership with OPEC in 1971, Nigeria has continued to take a firm control of her hydrocarbon resources, but has that been done efficiently and effectively?

The establishment of the NNPC and its operational mode of jointly developing fields and producing oil & gas through joint operating agreement via its subsidiary, the NDPC with the IOCs was seen as a means of involving the nation in tapping and utilizing her natural resource.

Accounting for 80% of the government earnings, through crude and LNG export, the oil and gas industry has been the economic front burner for the nation and indigenous players are now seeking to show competence and increase their presence as active players.

The Local players

The rise of the indigenous players such as Oando, Seplat, Niger Delta Western, First Hydrocarbon Nigeria, Conoil, have proven successful in marginal brownfields.

Other indigenous companies who have proven success in Nigeria with interests and partners outside the shores of Nigeria includes Oriental Energy, Shoreline Energy Resources, South Atlantic Petroleum, and Septa Energy Nigeria. 2013 entitlement resource and production in some of their fields are as below

Fig. 1 on page 7

The recent successful discovery of light oil accumulations in the Ogo-1 well on OPL310 is an encouragement on the resilience of the indigenous players showing ability to compete using local knowledge, technical ability through partnership with smaller international companies, and financial muscle to be successful.

Worthy of mention is the success of Elcrest – a JV between Eland Oil and Gas a London AIM company and Starcrest, an indigenous Nigerian company's redevelopment of OML 40 from Shell Petroleum Development Company of Nigeria (SPDC) in 2012. From a complete shut down by SPDC in 2006, they moved to a current output of 34kkbl/d, which shows the resilience of local players.

Shoreline/Heritage OML 30's redevelopment now grosses an average daily production of 35kkbl/d, compared to the outright shut down in 2007 when the asset was on SPDC's radar.

Frontier oil is a proven company seeking to harness the gas resources for local consumption through its OML 13 Uquo non-associated gas field, by solely supplying independent power plants for electricity generation.

2010-2012 saw the global players, Shell and Total divesting their onshore assets for

[1] EIA Country Analysis
http://www.eia.gov/countries/cab.cfm?fips=NI

Fig 1

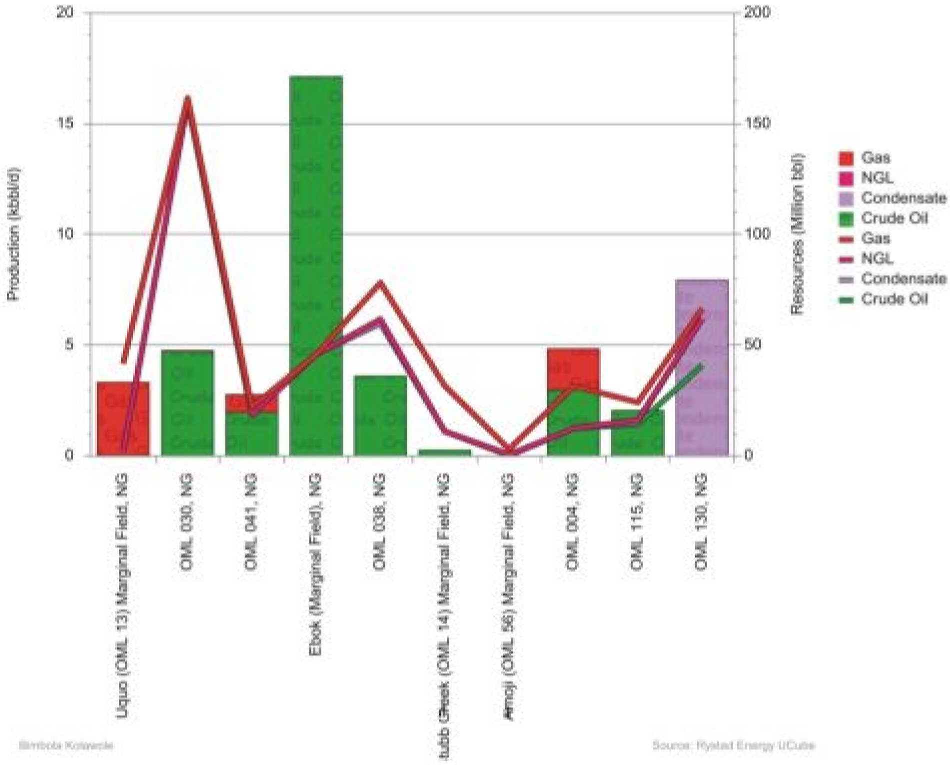
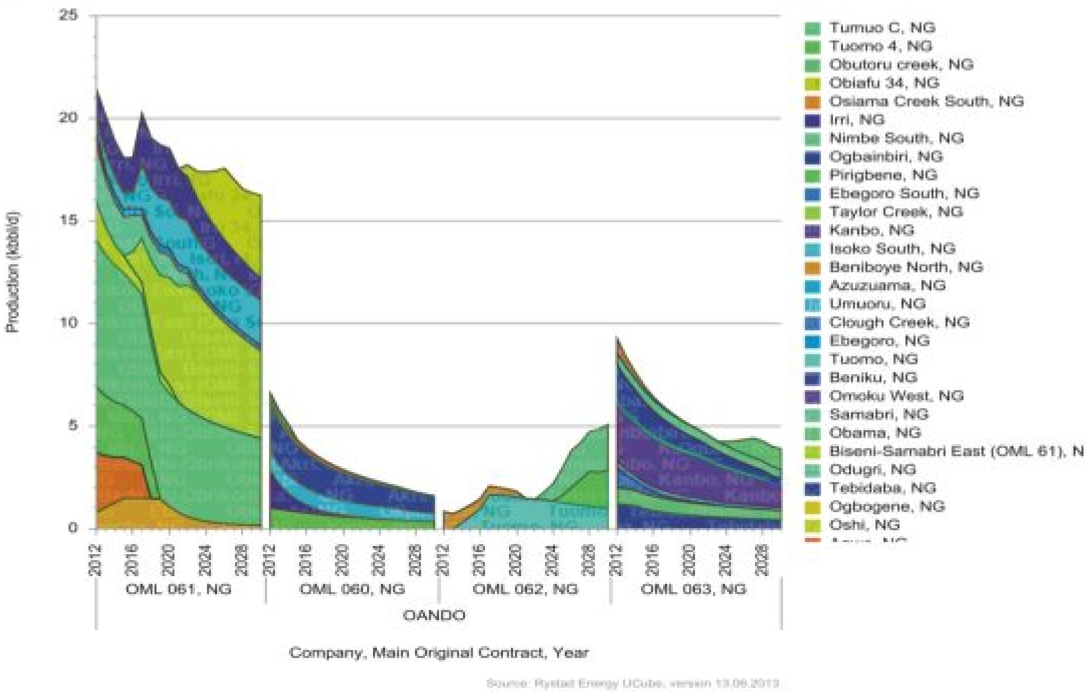

Production (kbbl/d)
Resources (Million bbl)
0
5
10
15
20
0
50
100
150
200
Gas
NGL
Condensate
Crude Oil
Gas
NGL
Condensate
Crude Oil
Uquo (OML 13) Marginal Field, NG
OML 030, NG
OML 041, NG
Ebok (Marginal Field), NG
OML 038, NG
Creek (OML 14) Marginal Field, NG
Amoji (OML 56) Marginal Field, NG
OML 004, NG
OML 115, NG
OML 130, NG
Bimbola Kolawole
Source: Rystad Energy UCube

Fig 2


Production (kbbl/d)
0
5
10
15
20
25
Tumuo C, NG
Tuomo 4, NG
Obutoru creek, NG
Obiafu 34, NG
Osiama Creek South, NG
Irri, NG
Nimbe South, NG
Ogbainbiri, NG
Pirigbene, NG
Ebegoro South, NG
Taylor Creek, NG
Kanbo, NG
Isoko South, NG
Beniboye North, NG
Azuzuama, NG
Umuoru, NG
Clough Creek, NG
Ebegoro, NG
Tuomo, NG
Beniku, NG
Omoku West, NG
Samabri, NG
Obama, NG
Biseni-Samabri East (OML 61), N
Odugri, NG
Tebidaba, NG
Ogbogene, NG
Oshi, NG
2012
2016
2020
2024
2028
OML 061, NG
OML 060, NG
OML 062, NG
OML 063, NG
OANDO
Company, Main Original Contract, Year
Source: Rystad Energy UCube, version 13.06.2013

focused activities offshore. Shell raised $1.8bn from exiting eight licenses, and the beneficiaries of such sales included Elcrest and Shoreline Natural resources.

2012 also saw Conoco Phillips leave Nigeria and sells all its assets consisting of 95% operated interest in the Chota field and 20% non-operated interest in the Uge field.

The deal also includes a 20% non-operated interest in OMLs 60-63, a 20% non-operated interest in the Kwale-Okpai independent power plant and a 17% non-operated interest in the Brass LNG project to Oando Energy Resources at a value of 1.79 BUSD with an anticipated final close date in mid-2013. **Fig. 2 See on page 7**

Petrobras is next to follow, with the hopes of investing it's proceed from the sale at an estimated value of 1.5 BUSD or 57,000 USD per barrel of production to finance Brazil pre-salt developments into assets abroad.

The latest IOC reducing her footprint in the Nigerian shore is Chevron Nigeria limited (Chevron).

Chevron's 40% interest on OML 83 and 85 is on sale. Additional assets to be equally placed on sale are OMLs 52, 53 and 55.

Chevron said it would prefer to sell to local Nigerian companies which fall in line with the local content regulation laid by the government. These sales at 'discounted' prices should be a wakeup call for serious indigenous players.

Growing Challenges

New resources discovered per year in Nigeria have declined in the last 10 years and during the last 5 years, less than 20% of the annual production has been replaced by discoveries. The challenges leading to this decrease in exploratory activity could be largely seen as no license round bid has taken place for 10 years. This also includes other matters such as the delayed passage of the PIB. A potential forecasted production decline from 2026 is seen in **Fig 3 chart on page 9**

While Fig.4 shows the life cycle of the assets and drives home the challenges looming ahead if exploration activities is not boosted: **Fig 4 on page 9**

Other challenges are:

- North America's unconventional resources. The recoverable reserves of NAM's shale oil &gas and tight liquid is an estimated 104Bbbl and a current total production of 13mmbl/d for the top ten assets which includes, Permian Delaware, Niobrara Shale and Western Gulf Province.

The US is becoming self-sufficient and this in effect will not only affect OPEC and its price regulations, but Nigeria in particular who has had the US as one of the main consumers of the sweet crude for decades.

Perhaps it high time alternative markets were searched.

- Inadequate technical and financial capacity of the growing indigenous players along with the rising cost of field development. Most of them already partner with smaller international companies; perhaps they can learn from these partners and eventually become fully independent.
- Above ground risk issues such as pipeline vandalization- includes most of the infrastructures being owned by the IOCs for crude oil evacuation, personnel security issues, force majeure and other associated

[2] Rystad Energy UCube
[3] Financial Times : http://www.ft.com/cms/s/0/abc2c026-da91-11e2-8062-00144feab7de.html#axzz2XmBFysNd
[4] Africa Oil+Gas Report – Oando's expensive route to 25,000BOPD
[5] Rystad Energy UCube

Fig 3

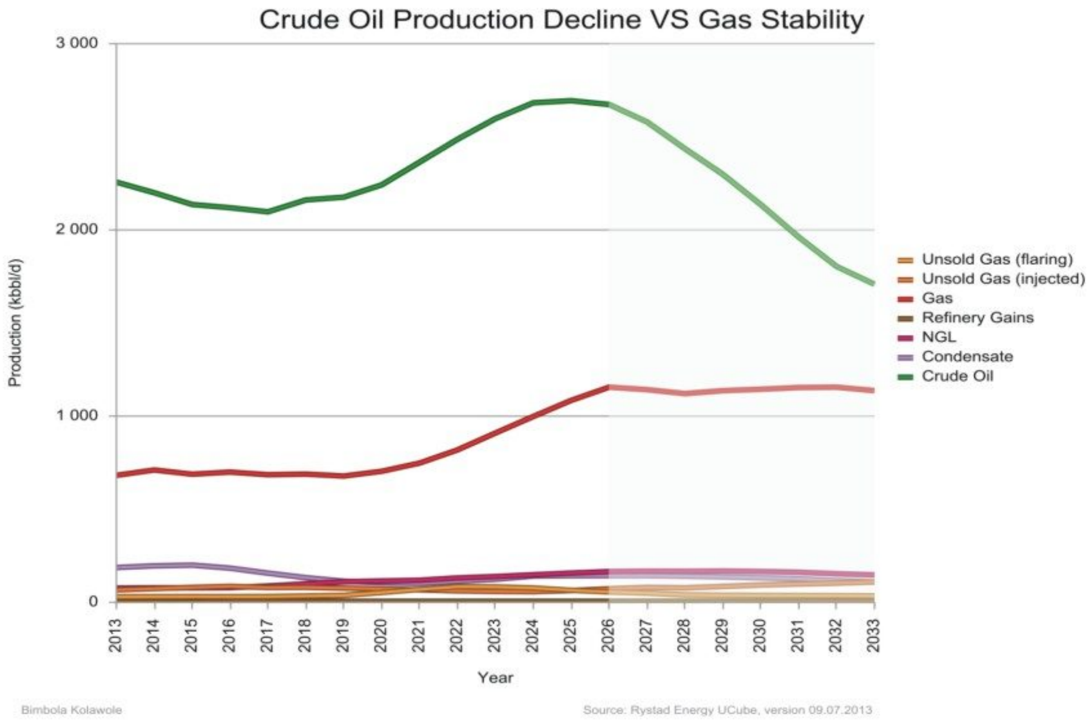
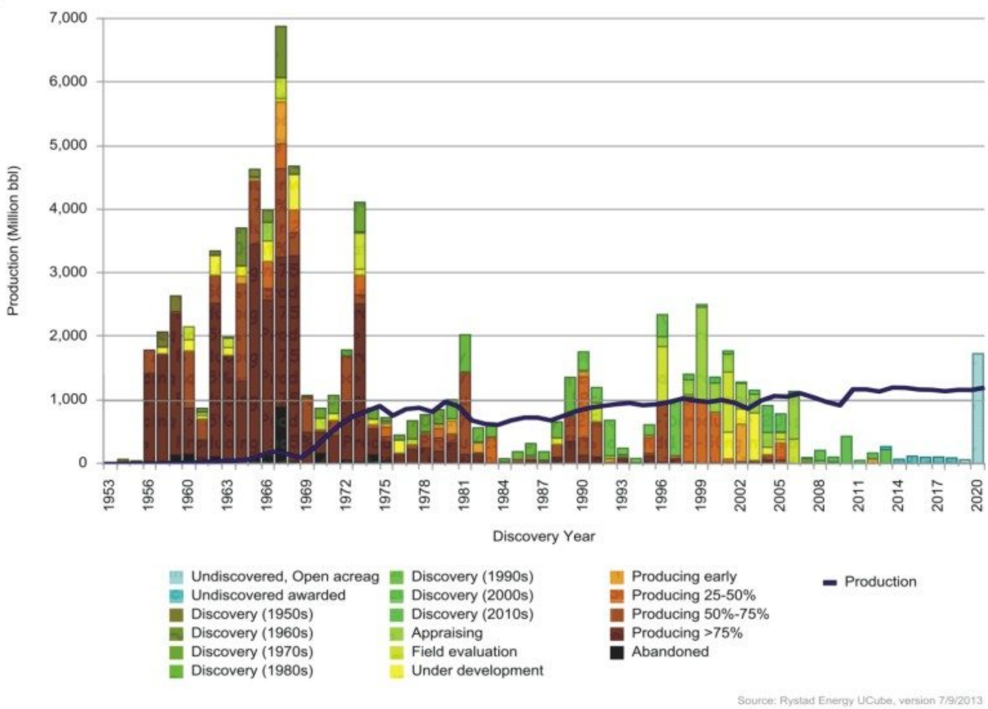

Crude Oil Production Decline VS Gas Stability
Production (kbbl/d)
Year
Unsold Gas (flaring)
Unsold Gas (injected)
Gas
Refinery Gains
NGL
Condensate
Crude Oil
Bimbola Kolawole
Source: Rystad Energy UCube, version 09.07.2013

Fig 4


Production (Million bbl)
Discovery Year
Undiscovered, Open acreag
Undiscovered awarded
Discovery (1950s)
Discovery (1960s)
Discovery (1970s)
Discovery (1980s)
Discovery (1990s)
Discovery (2000s)
Discovery (2010s)
Appraising
Field evaluation
Under development
Producing early
Producing 25-50%
Producing 50%-75%
Producing >75%
Abandoned
Production
Source: Rystad Energy UCube, version 7/9/2013

costs. Involving the host communities through environmental awareness, job opportunities and training, and provision of basic amenities can reduce and eventually eradicate the above-ground risks.

· Fiscal Regime issues such as PSC agreements, royalty and profit oil tax agreements that would be favourable and encouraging to the indigenous players should be considered.

· High amounts of flared gas which could be converted to re-injected resource and also used for local power plants.

· Importantly, local players must make effort to develop assets they have been awarded. In a challenging industry, the local players must be adequately equipped to operate as an independent entity

· Importantly, the host communities of these marginal fields should be carried along and made to feel safe and comfortable in their own environment.

Future Facts?

Though exploratory activities might seem dwindled on the lower side, there are lots of on-going activities in the oil and gas terrain of Nigeria and the indigenous players are not in the least conceding their abilities.

Indigenous players should be encouraged to establish infrastructures, building pipelines and local refineries. Companies such as Seplat /NDPC have a pipeline which runs from Amukpe to Forcados. This increases economies of scale and invariably becomes a cost effective method of getting the crude and gas to market and off-takers, and the ripple effect to a lower pump price. Eventually, these cascades to a thriving economy as its effect impact other sectors such as agriculture and finance.

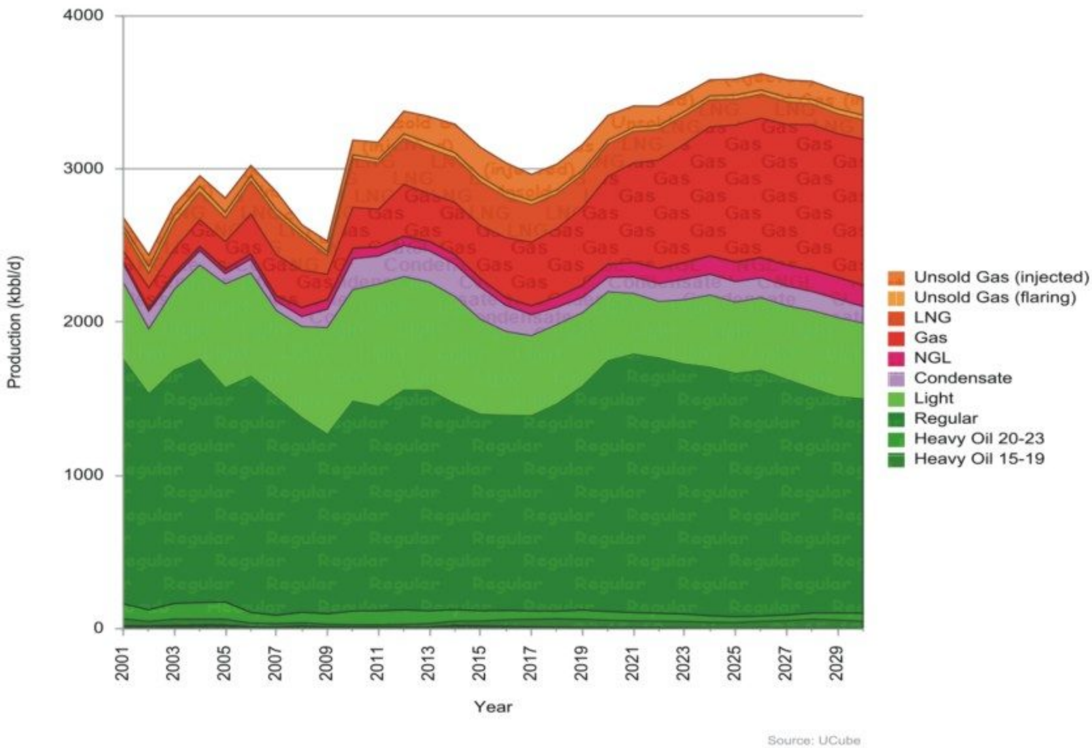
With a current total production of 3.5 mmbl/d, and a decline in 2015 due to several FPSO falling off plateau, Nigeria is yet to reach her full potential from the estimated 3.7Bbbl of reserves. It is reasonable to expect a growth in gas production from 2020-2026; there are opportunities to continue to harness the gas resources for power generation and re-injection for efficient oil production. All of these point to the fact that Nigeria is still very much the leading African player in the oil and gas sphere.

Fig 5 on page 12

Perhaps we should start doing things differently; after all, Nigeria is rich in not only resources, but also in People.

Africa Oil+Gas Report : Nigeria Vandals drains profit out of marginal fields
Rystad Energy UCube
EIA Country Analysis: http://www.eia.gov/countries/cab.cfm?fips=NI

Fig 5



RYSTAD ENERGY

Bimbola Kolawole is responsible for Rystad Energy's new sales and account management in Africa. Her expertise includes business analysis and development, strategy, risk management as well as project management.

Bimbola commenced her career at Vmobile/Celtel (now Airtel Nigeria) and continued later at IHS as an Energy Account Manager covering the geographical areas of Africa, the Middle East and Europe.

She holds a degree in Economics from University of Ilorin, Nigeria, an M.Sc. in Energy Finance from CEPMLP-University of Dundee, Scotland and an MBA from University of Leicester, UK.

HOW NEW LOCAL BANKING PRODUCTS CAN FAST-TRACK THE GROWTH OF "WORLD-CLASS" INDIGENOUS COMPANIES IN NIGERIA'S OIL AND GAS INDUSTRY

by Anthony Okolo

Nigeria owes most of its profile to its massive population and its importance in oil and gas production.

Following its first commercial oil discovery in 1957, Nigeria's production has grown steadily and quickly making her a formidable force within OPEC and a world with politics fuelled by the need for energy from crude oil. The nation's daily production capacity stands at about 2.2 million barrels per day, and proven reserves of oil exceed 37 billion barrels.

Despite these impressive statistics, Nigeria's oil wealth has not translated into riches for its people, nor has it produced an advanced technology environment or improved the state of its infrastructure.

A major reason for this is that majority of the yearly industry expenditures totalling over $18bn USD per year, escape the domestic economy in a phenomenon referred to as "capital flight".

It was in a bid to arrest this phenomenon that various governments and legislation have focused energy laws on limiting avenues for capital flight, culminating in the Nigerian Oil and Gas Content Development (NOGICD) Act 2010. Years of investment in human capital development by the Nigerian National Petroleum Corporation (NNPC) and its joint venture and PSC (production sharing contract) partners, coupled with advancements in various local content initiatives, have helped create a layer of highly competent and experienced Nigerian professionals including engineers, geologists and technicians who have worked their way up the industry ladders and even honed their skills working in Europe, the US and Asia.

Some of these professionals have embraced the new opportunities created by the NOGICD Act to establish a number of indigenous companies. However, the appearance of these companies on the supply chain landscape has failed to stem the flow of capital flight out of the country.

For the oil producing company, the critical nature of petroleum operations and the high risk associated with crude oil exploitation combine to ensure that none but the best materials and components can be deployed in the high technology search for oil and gas.

These factors often militate to bar entry for many indigenous companies as they are not usually considered "best in class" for the products and services they offer.

For example, an Umbilicals contract recently awarded by an international oil producing giant will see a substantial part of the entire scope performed outside Nigeria, due to a lack of world-class service companies and suppliers for key components of the work in-country. Even projects operated by

Press release: Aker Solutions Signs Umbilical Contract with Exxon Mobil,
http://www.akersolutions.com/en/Global-menu/Media/Press-Releases/All/2013/Aker-Solutions-signs-umbilical-contract-with-ExxonMobil/
Table 1: Nigeria experiences $380billion capital flight culled from www.vanguardngr.com April 23rd, 2013
See more at: http://www.vanguardngr.com/2013/04/nigeria-experiences-380bn-capital-flight/#sthash.YVTqEPzd.dpuf

indigenous oil prospecting companies fall victim to the phenomenon of capital flight, as lack of local supply capacity remains a recurrent theme.

It is tacitly understood that local supply capacity by the indigenous companies' is generally poor because of the lack of financial muscle to obtain technologies, equipment, personnel and processes.

CAPITAL FLIGHT IN NIGERIAN OIL AND GAS INDUSTRY (PRE-NOGICD ACT)

DELIVERABLE	CONTINENT	VALUE
Procurement	Asia	$39 billion
Technical Services	Europe	$117 billion
Fabrication	North America	$223 billion

Previously, it had been mooted that Nigerian banks lacked the financial base to make any meaningful impact on local content development. Indeed many of the nation's largest banks are unable to match the capital base of their foreign counterparts when energy financing is to be considered.

Most Nigerian banks operate in a dilemma-laden territory as most indigenous contractors have no proper business structure. Others are not really in the longevity business, as sporadic contract gains are preferred to long-term sustainability planning for the business. This has greatly hampered local banking support for an expanded manufacturing base, creating a lack of small and medium-sized enterprises capable of supplying the market for quality fabricated goods for oil and gas exploitation.

For the more focused and properly structured indigenous company, Nigerian banks can and do provide a variety of banking products aimed at assisting their business aspirations and plugging the gap in locally supplied goods. Some of these products made popular through their common usage are:- Local Purchase Order (LPO) finance; Invoice Discounting; Term Loans and Overdrafts.

LPO financing involves the provision of short term finance to small and medium scale retail customers with annual turnover of N500 million and below facility to carry out supply orders. The supposed maximum tenor of 120 days with an option to renew, usually for 60 days after the expiration of the facility is rarely the case as more realistically, banks seek to mitigate their risk by going for shorter tenures, usually 90 days with a 30 day extension .

The facility grant usually does not exceed 70% of the value of the supply order which can be in any of the recognized main currencies. The key requirement however is the Irrevocable Tripartite Domiciliation agreement which ensures that the bank has unfettered access to the contract proceeds from execution of the contract by the beneficiary company which will be lodged in an account held at the bank.

The main advantage of LPO finance lies in its ability to grant qualifying indigenous companies access to additional working capital which should, in practice, support growth and expansion. However, it is a source of concern that banks often seek additional comfort in form of collateral to approve applications for LPO finance thereby making it a difficult instrument to access by any other than the most asset-rich indigenous companies. Also, the short-term nature of the instrument which is usually open for an operative maximum of 90 days, ensures that the instrument is more suited to quick procurement contracts. Now we look at invoice discounting which is merely a banking

First Bank of Nigeria website http://www.firstbanknigeria.com

Esisal Lemuel 2009, Financing Options for Small and Medium enterprises (SMEs):

product that allows the invoice discounting company (discounter or invoice discounter) to buy the trade debts (also known as accounts receivables) of the business at an agreed funding rate, usually between 20%-25% on Naira receivables and 10%-12% on USD receivables. Discounters typically advance 80% to 85% of the face value of valid invoices. Making use of an invoice discounting can improve the bottom line of indigenous companies through a range of benefits, such as:

· Improved cash flow by releasing up to 85% of funds against the value of outstanding invoices.

· Access to an ongoing supply of cash that grows as company sales grow.

· Management time is freed to drive the business forward as receiving companies can spend less time on unpaid accounts and are no-longer held back by insufficient cash flow.

As with LPO financing, the reality does not mirror the promise of theory. The high interest rate militates against its widespread usage, and while it offers some comfort for short-term liquidity, delayed payments as a result of project overruns and delays (not at all uncommon in the oil and gas manufacturing sector), usually have unpleasant repercussions on the borrower, sometimes even leading to the winding up of the company and the loss of further indigenous capacity.

Term Loans as a credit facility legally commits the borrower for a specified amount, tenor and rate to finance specific transactions, capital projects or a customer's expansion programme with pre-agreed repayments schedules. However, the requirement for collateral in form of high value properties limits the eligibility for such facilities to all but the few companies who will gain little benefit from additional funding to their already robust financial capability.

Companies are also less likely to benefit from overdraft facilities as even though a line of credit which allows a customer write cheques for more than the actual balance on the customer's account with a finance charge on the excess, the requirements for eligibility require similarly prohibitive conditions The tenure of 1 year while attainable when added to this interest requirement, makes this a less attractive facility for smaller indigenous companies. The realization that these products are inadequate leads to a further investigation as to why they are unable to assist real growth in the Nigerian oil and gas industry.

To bridge this gap (which still exists today), Nigerian banks have to develop a better understanding of the day-to-day running of the indigenous oil company in the context of the local industry and also understand how the global industry influences demand and supply in the local environment. When this understanding is gained, the high-risk moniker that most banks tend to assign indigenous companies becomes less meritorious and the term "Emerging Giant" more descriptive.

Most high value oil and gas contracts are for the manufacture, fabrication, assembly and testing of oilfield components, which are often integrated into modular products for deployment in the field. As most manufacturing capacity is domiciled outside Nigeria and located in a few oil and gas centres in the world, capacity is stretched through global demand for similar products, causing production lead times to oscillate between 3-4 months for small items to up to 18 months for more critical production systems. It is this high value manufacturing capacity that creates real

First Bank of Nigeria website http://www.firstbanknigeria.com

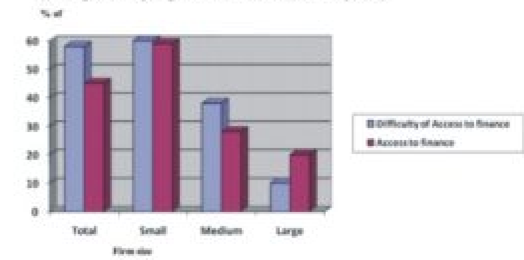
Esisal Lemuel 2009, Financing Options for Small and Medium enterprises (SMEs): Exploring Non-Bank Financial Institutions As An Alternative Means of Financing - The Case of Nigeria.

technology transfer and gives companies the experience in delivery of quality products which move them from local participants to Emerging Giants, capable of satisfying global demand. This shift however, cannot be achieved without access to medium-term finance.

If one can extrapolate a recent report by the CGAP on the indigenous company scenario in Nigeria, one finds that despite the large percentage of indigenous oil and gas companies operating in the country, only about 5% of them get access to loans from banks despite the fact that 80 percent of them seek financing (CGAP: Access to finance in Nigeria report, 2009) . The figure below depicts the extent to which access to and cost of financing are a problem for Nigerian firms, according to a report from an ICA study in 2008.

FIG 3: Difficulty in Accessing Finance and Cost of Debt- Nigeria

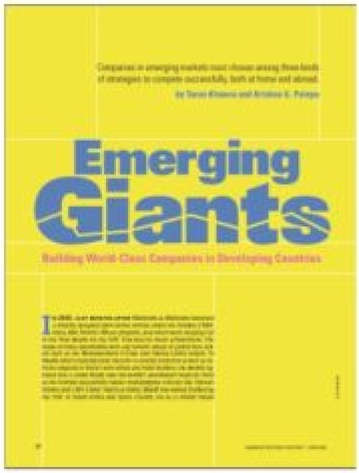
(Percentage of firms reporting access to finance and cost of debt as a problem)



Source: ICA Report (2008)

According to a study by Harvard University in 2007 (HBR 2007, Emerging Giants - Taroun Khanna and Krishna G. Palepu), at first glance, European, US, and Asian companies appear to hold clear advantages over indigenous companies.

Even the multinationals possess well-known brand names, strong research and development processes and sophisticated technologies it is their access to vast reservoirs of low-cost finance and talent that sets them apart from their indigenous counterparts in



this case. These companies, for instance, can raise large sums of money to fund new equipment acquisitions and developmental projects to increase capacity at a low cost because of their well-established financial markets which they can apply in lowly industrialized nations such as Nigeria as multinational companies. It is this quality that allows them to attract the best brains to their companies, and mostly endears them to the Nigerian bank as prime lending candidates.

What local banks fail to realise though is that multinational companies from the developed world must confront the same institutional voids that indigenous companies face with regards to lack of infrastructure and skill gaps. The advantage swings to indigenous companies however when it is realized is that these multinational companies are ill equipped to deal with these institutional voids and therefore find it almost impossible to expand operations in the country, creating huge gaps in capacity within the local industry, which in turn, create a huge financial opportunity for local companies who are more adept at navigating these institutional voids, using their familiarity with the local context to identify and meet customers' needs effectively at a premium.

Many emerging-market companies have become world class businesses by capitalizing

Tarun Khanna and Krishna G. Palepu 2007, Emerging Giants: Building World-Class Companies in Developing Countries.
Esisal Lemuel 2009, ibid

on this knowledge of local product markets to create profitable conglomerates and earn the "Emerging Giant" description. These emerging giants have also exploited similarities between geographically proximate developing markets to grow across borders.

This insight into how emerging giants are created provides the recipe for local banks to develop products that match this ability to turn the lack of local capacity into a price advantage. One of such ways to do this, is to look at hitherto un-fancied medium-term financing strategies such as the finance and operating lease structures. In the Finance lease, the lessee is transferred all the risks and benefits of ownership, while the Lessor retains the title of the equipment .

The lease is usually non-cancellable by either party before the expiration of the primary tenor and payments are sufficient in total to amortize the capital outlay of the lessor and to provide for the lessor's cost of funds plus a desired return. In operating lease, the asset is not fully amortized during the primary tenor. The lease is therefore usually shorter than the estimated useful life of the asset and can be leased out on a secondary lease. Local banks have historically avoided creating lease products but may be cajoled to have a re-think when a closer investigation by ELAN (Equipment Leasing Association of Nigeria) reveal that most leasing companies are able to access loans from the financial system and provide a final interest repayment cost to the indigenous company customer of between 35% - 50%. Any intervention by the local banks to cut out the middle man in this leasing transaction could easily attract between 23%-25% in interest repayments direct from the lessee. This represents a marked improvement on the interest margins for LPO financing loans and other financing alternatives discussed earlier.

The second suggestion is that local banks open venture capital departments whose main task is to identify indigenous companies which provide a value proposition for the oil and gas industry and then provide the financing to transition them from local participants to emerging giants, with considerable upside in the process.

The main concern for banks will as always be the larger risk portfolio which the Venture Capital Department (VCD) will have to assume but with the increased availability of in-house and third-party professional support from many seasoned industry professionals and firms, the supervisory function which is required for the banks to monitor and guard its investment is not as difficult as it once was.

From the foregoing, is obvious that there are plenty of products and strategies that local banks can develop to assist the growth of indigenous companies by making available the funds for them to compete more favourably with their multinational counterparts and grow them into Emerging Giants.

It is now also apparent that to do so, the input of professionals and firms who understand the inner workings of the industry and who are experienced in identifying risks and opportunities is essential to providing these products. When these two assertions are put together, the result is that local banks must create a higher appetite for risk-based lending which promises higher reward for National Development, Local Content and makes complete sense in terms of dollars and cents.

NIGERIAN MARGINAL OIL FIELDS; THE KNOTS IN FUNDING

by Wale Shonibare,
Managing Director, Investment Banking at UBA Capital Plc.

Interesting to note that Nigerian indigenous firms own more than 50% of the 173 oil and gas concessions in Nigeria so far, but accounts for less than a tenth of the 2.3 million barrel/day production; a paradox of "idle wealth", that has denied the Nigerian government and people the full benefit of local participation policies.

More precisely, the 32 marginal fields awarded (inclusive of the 5 discretionary awards and NPDC's fields) cumulatively produce c.2.6% of daily oil production and 2.5% of the estimated 4,000 MMscf gas production in the country, due largely to the inability of indigenous firms to fully monetize the assets. Good to note that marginal oil fields as defined in Nigeria are oil fields or wells that are nearing end of commercial life and whose production rates are lower than 10,000 barrels per day.

Whilst noting the dearth of local technical expertise, given decades of isolated IOCs participation in the upstream oil and gas sub-sector, we think the inability of indigenous marginal field owners/operators to secure adequate funding is a core bane to unlocking the underground wealth, especially to achieve "first oil". With a March 2015 ultimatum for all marginal field licensees to accomplish optimal operation, we track the salient facts undermining the monetization of these assets.

Whilst the erstwhile aversion of the Nigerian banking system towards long tenored project finance in the upstream oil and gas sub-sector was a notable barrier to financing, beneath the funding challenge lies the bankability of the assets, given a host of "soft points" that encumbers the economics of the fields.

To start with, the award process, which joins "strange bird fellows" encumbers the asset from the onset, as such fields end in years of litigation. More so, the inaccuracy of the reserve data (beyond tolerance limits), on which the fields were awarded undermines the bankability of the projects.

Closely tied to the fiscal process of field awards is the adverse selection of technical and foreign equity partners, leading to inconsistency in field development and production, given fluctuating service level agreements and lopsided cost and earnings sharing negotiations.

Whilst farming has been a traditional source of equity funding for marginal fields, it leaves the indigenous firms at the mercy of foreign equity and technical partners, with less interest in marginal fields, an unbalanced alignment of interest, which slows down the field development.

More importantly, the dearth of financial and project advisers on marginal fields have undermined the investment case for accessing funding, especially as the project economics is often fraught with complexities and inconsistencies surrounding taxation, pricing, capital expenditure and funding terms.

Nonetheless, the recently steep trend in local capacity development, engineered by a new generation of indigenous talents with a good match of enterprenuerial and technical skills should be positive for the increased contribution of marginal fields to overall oil and gas production in Nigeria.

Interestingly, recent success stories and the track record of these experienced locals in translating reserves to cashflows is steadily improving the appetite of local banks for marginal field financing just as local capacity development of local project finance advisers like UBA Capital and a few peers should provide support for marginal oil and gas project development, going forward.

Albeit, in achieving the fiscal local content drive, relevant government agencies need to address the fiscal-related constraints in the awards of oil fields as well as ensure concessional tax regime for marginal field development, given elevated marginal operating cost of the wells. Investment Rating Criteria and Disclosure UBA Capital Research adopts a 3-tier recommendation system for assets under our coverage: Buy, Hold and Sell.

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We consider this as the minimum return that may deserve our holding of a risk asset, like equity, especially as we consider the average 4.5% total transaction cost for an average retail investor.

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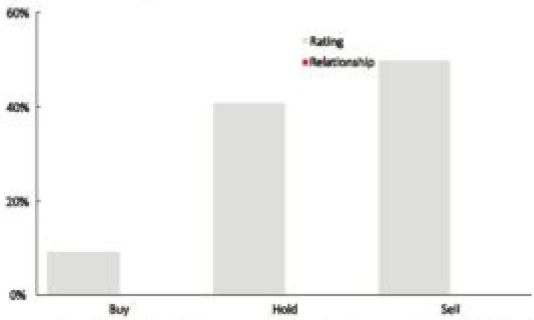

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Wale is the Managing Director, Investment Banking at UBA Capital Plc. He has over 22 years experience of Infrastructure finance and development spanning Asia, Europe, Middle East and Africa. Prior to joining UBA Capital, he was Managing Director and Head of Infrastructure, Africa, Middle East and New Markets at Renaissance Capital. He has also worked with KPMG as a Director in London and Dubai.

Wale is responsible for UBA Capital Plc's Investment Banking business which spans Debt and Equity Capital Markets, M&A, and Project Finance. Recent experience includes state government and corporate bonds, project and structured finance and M&A transactions across various sectors: Power generation and distribution facilities, upstream oil and gas, CNG and LNG facilities, fertilizer plants, hydropower power projects, coal mines, toll roads, light and heavy rail, ports, real estate and hospitality and specialized economic zones.

Wale holds an MBA from Imperial College, University of London and a B.Eng (Hons) degree in Civil Engineering from the University of Glasgow.

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Argentil is a leading Nigerian boutique advisory and investment banking firm with a focus on the energy and infrastructure sectors. Since inception in 2002, we have acted as Transaction and Financial Advisor and Lead Arranger on major power and infrastructure projects valued in excess of US$3 billion.

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Foreword by Rumundaka Wonodi (NBET)

This Journal is a welcome addition to the emerging literature on the reformed power sector in Nigeria. While there several journals focused on the oil and gas, this journal extends energy rightly to add electric power to the mix. More than half of the articles in it are dedicated to the sector reform, a clear indication that this is the next frontier for Nigeria's private sector. The Nigerian Electricity Industry is Nigeria's newest industry in the sense that the conclusion of the privatisation of the unbundled Power Holding Company of Nigeria (PHCN), with the handover to new owners on November 1 2013, fully brought about the dawn of a private sector led electricity market.

The Sector reform process started in 2001 when the Federal Government adopted the National Electric Power Policy. Four years later, in March 2005, the Electric Power Sector Reform Act (ESPRA) was passed into law. A key thrust of the reform was the transfer of the control and ownership of the industry from the public sector to the private sector. The Act, inter alia, saw the creation of PHCN which assumed the assets, liabilities and employees of the erstwhile Nigeria Electricity Power Authority (NEPA); the subsequent unbundling of PHCN into 18 successor companies, establishment of an independent regulator, Nigerian Electricity Regulatory Commission and the subsequent establishment of the Nigerian Bulk Electricity Trading Plc. (NBET).

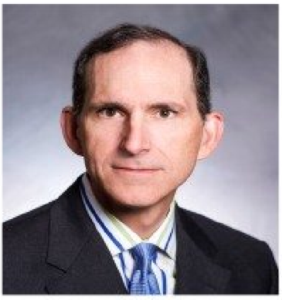
The ALP Energy Review articles achieve a tripod effect. It provides the chronicles of the final stage in the reform process, it frames the discussions on the issues and helps define the narrative for future discussions.

I applaud this maiden edition of the ALP Energy Review as it truly captures the spirit of the final phase of the reform process of the last three presidential administrations, and sets the stage for the newly privatised sector.

Congratulations to the ALP Team!

Rumundaka Wonodi
Managing Director and Chief Executive Officer
Nigerian Bulk Electricity Trading Plc.
Aka The Bulk Trader

NBET
NIGERIAN BULK ELECTRICITY TRADING PLC



ELECTRICITY RESTRUCTURING IN CANADA AND THE ROLE OF ITS BULK TRADER: POTENTIAL LESSONS FOR NIGERIA?

by Ron Clark and Ajeet Grover, Aird & Berlis LLP, Toronto, Canada

On June 3rd of this year Reuters news agency reported new developments in the restructuring and privatization of Nigeria's electricity industry. The Federal Government of Nigeria had announced plans to sell 10 gas-fired power plants, totaling 5,000 MW in capacity, to private investors. While such news came on the heels of the much larger development in late 2012 with respect to the sale in the stakes of several generation and distribution companies unbundled from the successor to the former state monopoly, the National Electric Power Authority ("NEPA"), combined these developments highlight the commitment of the current administration of President Goodluck Jonathan to implement its power sector reform policies, as set out in the 2010 Roadmap for Power Sector Reform and the 2005 Electric Power Sector Reform Act.

The unbundling of NEPA and commensurate privatization of state power assets are important steps in Nigeria's road map for a competitive and predominantly privately owned electricity industry. However, lessons from Ontario, Canada's experience with electricity restructuring suggest that the Nigerian Bulk Electricity Trading Plc ("NBET") could play just as an important role in determining the eventual outcome of the government's power sector reforms and, in particular, the success of a competitive wholesale power market.

In several respects, Nigeria's electricity sector reform programme has followed that pursued by Canada's most populous province, Ontario, in the late 1990s. Ontario Hydro, the state controlled power generation and transmission monopoly, was unbundled into several entities, including an assignment of its liabilities (including stranded debt from Nuclear projects) to the Ontario Electricity Financing Corporation, a state controlled corporation similar to the role to be played by the Nigerian Electricity Liability Management Company.

In 2004, a newly elected Liberal Ontario government caused the creation of the Ontario Power Authority ("OPA") as a special purpose non-share capital statutory corporation with functions in several respects similar to NBET.

But while NBET was conceived as a precursor and stimulus to the establishment of competitive bilateral power markets and power exchange, the creation of the OPA was a creature of political necessity. The electricity market had opened in Ontario in May of 2002 but lack of generation resources and price spikes created public dismay.

The Conservative government of the day responded by freezing the retail price of electricity, in effect killing the retail market and removing incentives for investment. That government lost the next election and the new Liberal government created the OPA as a creditworthy central buyer to procure new electricity generation resources.

While the timing of the creation of NBET and the OPA differ, the policy intention with respect to both entities is the same: to provide independent power producers and other sellers of power with a creditworthy counter-party to power purchase agreements, and ensure that such agreements would be financeable by third-party lenders. For the OPA, creditworthiness is in large part a result of the Ontario Electricity Act, 1998 which enables the OPA to recover all of its costs and fees, including procurement costs, from Ontario rate-payers, rather than by direct government guarantees and other credit enhancement facilities provided to NBET (including by the World Bank).

With the OPA soon approaching its ten year anniversary, several important lessons may be taken-away by Nigerian legislators and policy makers with respect to NBET:

First, a bulk trader or "single-buyer" procurement authority can be very successful in a procuring large quantities of much needed electricity resources within relatively short time frames. As an example, during the 2005-2007 period, the OPA procured more than 8,000 MW of new (primarily gas-fired) generation; and over 4,600 MW of renewable energy supply resources were contracted for between 2009 and 2011 during the first phase of the OPA's Feed-in tariff program.

Second, if the government or a government department has close legislative oversight or certain powers over the direction and strategy of NBET, it could be used as a tool of public policy. While the OPA has management and a board of directors that are required to function independently of the Ontario government, the OPA's empowering legislation requires it to carry out energy conservation programs, undertake transmission and general power system resource planning, promote the take-up of renewable energy, and conduct procurements subject to the specific direction of the government's energy department (the Ontario Ministry of Energy). The OPA has successfully carried out these functions, however such public policy objects can at times work at cross-purposes to the OPA's role as a commercially oriented procurement entity.

A third and final lesson relates to the notion of a bulk-trader functioning as a temporary or "transitional" mechanism to facilitate wholesale competition. The extent of the success of a single-buyer in procuring megawatts on behalf of the government, and its utility as a public policy tool, may serve to entrench the entity as a longer-term player in the jurisdiction's electricity restructuring programme. As alluded to above, the OPA was initially conceived as a "transitional" agency whose purpose would finally be achieved by the loss of its relevance owing to the emergence of robust competitive power markets. In fact, to an extent, generators are very comfortable with their OPA contracts and there is no political will to phase-out the OPA.

With Nigeria currently at an earlier stage than Ontario with respect to its development of a competitive and private sector driven electricity industry, it has the advantage of learning from solutions and mistakes from early movers such as Ontario, including understanding the role that a bulk trader or single-buyer can play in the country's restructuring efforts.

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[1] Michael Wyman, "Power Failure: Addressing the Causes of Underinvestment, Inefficiency and Governance Problems in Ontario's Electricity Sector", C.D. Howe Institute Commentary: No. 261, May 2008, at p. 6.

[2] Ontario Ministry of Energy, Ontario's Feed-in Tariff Program: Two Year Report, Toronto: Queen's Printer for Ontario, March 19, 2012, at p.4.

AN INTERVIEW WITH MICHAEL LAKOTA.

CEO of SIEMENS Nigeria

Michael Lakota is MD of Siemens Nigeria, a role he assumed in January this year. He studied Economics and has been working in the Corporate Sustainability Department of Siemens AG for some years; developing solutions which address the global challenges presented by Megatrends – demographic change, urbanization, climate change and globalization.

How committed is your company to the country?

Siemens is deeply committed to the development of the electricity sector in Nigeria.

The Company has been delivering solutions across the entire energy value chain towards Nigeria's sustainable infrastructure development and economic prosperity.

Siemens built the 434MW Geregu I Power Plant and has also worked with several manufacturing companies to build captive power plants across the country.

Geregu I Power plant is the best-in-class of the PHCN generating plant; delivered on time and on budget with no fatalities. Siemens is currently building the Geregu Phase II project; expected to be commissioned by mid-2013.

In January 2013, as part of efforts towards strengthening its investments and market penetration in Nigeria, Michael Lakota was announced as the new managing director.

When you were asked to come to Nigeria what crossed your mind?

I was excited about my posting to Nigeria! Nigeria is a very strategic market for Siemens and we are keen to support the development of Nigeria's economy. I see a lot of opportunities in Nigeria, especially across the key sectors of energy, industry, healthcare and infrastructure development.

Siemens is uniquely positioned to provide answers to Nigeria's challenges across these sectors. We are committed to partnering with the government and the private sector towards deploying the innovative solutions, which Siemens is well known for in Nigeria.

What is your mission statement as the Chief Executive Officer of Siemens Nigeria?

Siemens is "In Nigeria for Nigeria" This is not just a nice slogan for Siemens; it defines how we do business in Nigeria. We are in Nigeria to make a positive impact on the economy; to provide sustainable solutions to Nigeria's challenges across the energy, industry, infrastructural and healthcare sectors and not here just for short term profits. A key pillar of our strategy is local human capital development.

Siemens Limited Nigeria recognizes the importance of knowledge and technology transfer and will therefore proactively seek

This interview was conducted by BusinessDay staff, Olusola Bello, and originally published on 21 March 2013, by BusinessDay.

out strategic opportunities to facilitate the growth of local human capital and local value add in the course of running its business.

How can the country achieve stable power supply?

I believe Nigeria is on the right path towards achieving stable power supply with the ongoing privatization.

The government and industry stakeholders just need to ensure that the process is followed through to the end. The power sector in Nigeria has come a long way; the landscape is changing with more private sector involvement and investments. With the completion of the ongoing privatization, there will be increased efficiency, transparency and ultimately customer satisfaction.

In a few years, I believe that we will begin to see the benefits to the entire population, including residential and non-residential electricity customers. Overall, the well being and quality of life of all Nigerians will improve, as a result of extended access to more reliable supply of electricity at improved quality and reduced cost.

Is Siemens in partnership with any of the investor that has bought the power distribution companies?

Yes, Siemens is actively involved in the ongoing privatization programme. We are technical partners to a consortium which has been announced as preferred bidder for one of the distribution companies.

We are also in advance discussions with some of the buyers of the Gencos. We are commited to bringing our global expertise, experienced and technology for running generating and distributing assetss to bear in Nigeria. We are very excited about being a part of the solution to the challenges in the Nigerian power sector.

What would you do if you are made the Power Minister in Nigeria?

First of all, I will focus on final- ising the ongoing privatisation process. I believe that while privatisation is good, it is not the only answer to Nigeria's energy challenges. There is a need to create an enabling environment for private sector investments in generation, transmission and distribution ca- pacities. I will strongly entrench a "maintenance culture" as this is the only way we can ensure that the industry investments are run sustainably. The ongoing NIPP projects need to be completed and the plants need to have access to gas.

Going forward, gas availability for power generation will be a key determining factor for the development of the sector. Without gas, you cannot produce power; no one will be willing to invest in a power plant without an assurance of gas supply. Access to gas could potentially limit the volume of investments in the sector over the next few years. To address this, the Ministry of Power needs to further improve their inter-ministry coordination with the Ministry of Petroleum and also NNPC.

My advice to investors is this: It is important to find the right partner. Find an experienced partner who fully understands the Nigerian environment, the best technology suited for the market and who also has a proven track record of success in this market. There is no market quite like Nigeria, there are unique challenges faced by project developers.

In 2006, Siemens built Geregu Phase I with a capacity of 414 MW. The ongoing Geregu Phase II project is on time, on budget and of perfect operational excel- lent, meaning that were no fatalities, nor major injuries. This something we are very much proud of. This is a success story that we always communicate to our potential investors, I would encourage the potential investors to go to Geregu and Ajaokuta and meet withour team of engineers. There are about a 1,000 people working night and day to bring the power to the grid.

How does your company intend to achieve the I0,000MW MOU signed with the Federal Government?

In April 2012, Siemens signed an MOU with the Federal Gov- ernment to build 10,000MW of electricity generating 2020. This is very ambitious but it is achievable. We have the full support of our management towards investing in Nigeria towards the achievement of this target. We are speaking with various project developers and we are also in close discussions with the Ministry of Power.

Before the end of this year, we expect to record the first power project to be implemented within the framework of the MOU.

What other programmes do you have?

We are passionate about the development of renewable energies. I believe that in some parts of Nigeria, especially the Northern part of the country, renewable energy would fit -in those places. I believe with proper maintenance, investment, and business plans this would be a reality. We are committed to partnering with project developers to optimise the country's renewable energy sources.

In what other areas of the economy are you involved in the country?

The energy sector is very important for us in Nigeria, as we see how we can support the country towards achieving its economic objectives. A lot depends on the success of Nigeria's energy sector from manufacturing to mining to communication to healthcare. However, Siemens is uniquely positioned to deliver solutions across four sectors - energy, healthcare, industry and infra- structure and cities sectors. Our energy portfolio covers integrated solutions covering oil and gas (upstream, midstream and down- stream); fossil power generation, renewable energy and power transmission and distribution. Our healthcare portfolio covers basic healthcare solutions and a wide range of diagnostic and therapy solutions. Industry port folio covers automation and drive technologies, while infrastructure and cities covers rail systems, mobility and logistics, low and medium voltage, smart grid and building technologies.

We see a lot of potentials for growth in the Industry sector because of the dynamic nature of the Nigerian market. With about 160 million people in this country; there is an extremely high demand of food and beverage products. So investment has to come in this sector. I strongly believe in the food and beverages sector.

We also see significant opportunities in the infrastructure sector with rails, airport and city solutions. This is a very dynamic country with a rapidly growing population of young people. I read about An astonishing number of about 20,000 moving to Lagos every day. So mega cities like Lagos need sustainable infrastructure development otherwise there is a risk that the overstretched infrastructure will one day shut down with significant cost to individuals, businesses and the country at large. The 20,000 people coming everyday need water, electricity, transport. In our city portfolio we provide metros, trains, light vehicles and electric power for surveillance operations.

EVALUATING THE POWER SECTOR

The Transaction and Financial Advisor's Perspective

by Gbenga Hassan, Àrgentil Capital Partners

Activity in the Nigerian power sector has grown significantlyover the last ten years. The establishment of Power Holding Company of Nigeria ("PHCN") and the 18 Successor Companies (see Figure 1) as a conduit for the government-held power assets by the Electric Power Sector Reform Act 2005 (ESPRA 2005) was the watershed. As Advisors operating in the space, with participation prior to the on-going privatisation, we witnessed this progression firsthand.

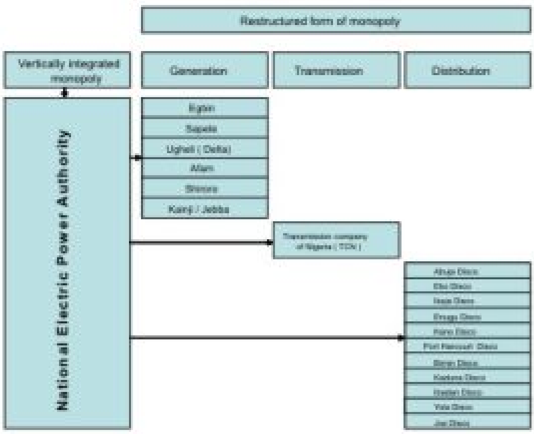

Figure 1: Institutional framework of sector

When we forayed into the sector, the challenges were immense. In addition to the Federal Government's seeming reluctance to relinquish its tight grip on the industry, the cursory participation of the lending community in the market was a major restriction. Notable fallouts of these are a dearth of information and the unwillingness of lenders to provide non- or limited recourse financing typicalfor utilities.

The need for reforms

The perennial widespread electricity power shortage,inefficiency and the attendant self-generation of power by consumersprompted the on-going reforms in the power sector.

Even with thedevelopment of 10 additional gas-fired power plants via the National Integrated Power Projects ("NIPPs"), initiated during the President Olusegun Obansanjo administration, there still exists a wide demand-supply gap.

In 2008, a report by the Director General of the Energy Commission of Nigeria (ECN), A.S. Sambo attempted to capture energy demand and the optimal supply capacity required to match demand. The projections were made using the International Atomic Energy Association modeling tools.

The results of this analysis for the reference scenario – assuming a 7% growth rate of GDP, are captured in Figure 2.

Figure 2: Power Supply Gap Analysis

The projected demand for 2015, using the reference scenario, was 28,360 MW. With peak generation to date stalled at 4,321MW, the shortfall is clear. Indeed, even if all of the country's planned capacity of electricity

generation is delivered, there will still be a gap between supply and demand in ten years' time.

In the right direction, however more throttling needed

Whilst credit to theprivate sector has increased about two foldin the past five years, the power sector has experienced a muted share in this growth, largely due to the lack of a robust and commercially viable framework for the sector. Culprit also, was the lack of a coordinated value chain approach to the sector by the government;creating weak links across the valuechain, and ultimately creating bankability concerns.

The failure of any on-grid IPP to come on-stream, in spite of the issuance of over 40 licenses by Nigerian Electricity Regulatory Commission (NERC), reflect these issues. Thus, until recently, participation by lenders had been confined to less risky small captive (off-grid) projects for off-takers (good credits, largely industrials), with Power Purchase Agreements ("PPAs") backstopped by corporate guarantees. Given that these power solutions are typically in the 1 - 20 MW range, the pace of progresscould at best be described as the proverbial first steps of a thousand miles.

Thankfully, there has been more thought and steps taken by the government towards a coordinated approach to de-risking the value chain. One of the many critical actions was the development in 2008 of a cost reflective tariff trajectory for the sector, the Multi Year Tariff Order ("MYTO"), and a subsequent revision in 2012. Given that the success of the MYTO is hinged on an efficient and liberalised market structure, there has been increased pressure on the government to complete the privatisationprogram that commenced in 2011 for the government dominated sector.

The privatisation process for the Generation and Distribution (excluding transmission) segments has opened the sector to investors who previously had minimal access, and provided tools for assessing investment in the Nigerian power value chain. Importantly too, this sale of PHCN assets worth approximately US$2.56billion has offered the local lending community an unprecedented opportunity to enhance their understanding of the sector, as they partner with experienced local or offshore banks, ultimately preparing them for the anticipated increased sector activity.

The MYTO II methodology,with its robust macroeconomic(inflation, exchange rate, etc.) and project level assumptions (construction costs, cost of capital, etc.) has provided a good head-startpost implementation in July 2012. Participation in the privatisation process and new IPPs being developed have been hinged on the cost-reflective tariffs inherent in MYTO.

The power sector at the tipping point

Indeed events in the ongoing reforms, via the privatisation process would to a large extent dictate the course of the sector and

[11] National System Operator Daily Report (27-03-13); Sambo, A.S. (2008). Matching Electricity Supply with Demand in Nigeria. *International Association for Energy Economics, 32-36.*
[12] Bankers Committee National Retreat, December 2010

provide much needed demonstration effect to spur further private sector participation in the sector's value chain. Essentially, the sector cannot afford a failed privatisation, and must ensure that the process receives as much support as possible. Admittedly, the PHCN privatisation process has had a fair share of issues; notable of which isa perceived"rushed" assetdue diligenceperiod.

Moving forward however, one expects that the lessons learned from the PHCN privatisationwould be brought to bear on the current NIPP privatisation, and we thus hope for a better organisedround of assets sales.These will also be supported by continued strengthening of institutional frameworks such as Gas supply---where progress has been made so far, with the development of a strategic gas aggregatorvia the Gas Aggregator Company of Nigeria ("GACN") and an aggregated price, as well as Transmission capability via the Transmission Company of Nigeria (TCN).

For transmission, a vital connecting point along the value chain, the planned retention of the transmission link within government control in the privatisationprocess leaves few financing options on the table in the government's quest to raise the estimated US$5.5 billion capital expenditure required. Given that the grid is constrained at wheeling just c.5,000MW, strengthening this linkage simultaneously with other reform initiatives is pertinent, ahead of the expected ramp up in generation capacity.

The government has recently issued aUS$ 1billionEurobond, which is to support the power sector reforms, including capitalisation of the Nigerian Bulk Electricity Trading Plc. ("NBET") and investments in gas and power transmission infrastructure.

Practically, given the untested commercial framework of the sector, government's participation will go a long way in de-risking the transmission segment, and herald other innovative financing strategies e.g. PPPs, JVs, etc.

Even so, crucial to private sector participation in the transmission space is the assurance of cost recovery (and returns) through the transmission tariff. Given its current subordination on the sector cash waterfall, this is exposed to the tail-end collection and reimbursement risks of the distribution companies, thus buttressing the need for initial government expenditure at this delicate period with elevated Aggregate Technical, Commercial and Collections (ATC&C) losses.

One suggested model for implementation post-transition phase (when ATC&C losses have been reduced), is the concession of the Transmission grid (possibly for a duration of 15 – 30 years) to capable parties who would cater for the expansion capital expenditure, and would be assured of cost recovery through the transmission tariff, as well as government support with respect to reducing Right of Way concerns.

Waiting for pay day

The ultimate success of these reforms will depend on the profitable and sustainable flow of funds through the sector value chain. Central to this, is NBET, which is the governmententity charged with paying the generating companies ("GenCos")for power off-take through long-term PPAs.

The bulk of NBET's liquidity is expected to comefrom collections of the DisCosduring this transition phase. However, there areliquidity and capital adequacy concerns

[13] The TCN is being managed under an initial 3 year Management Contract by Manitoba Hydro of Canada

surrounding the NBET, particularly with respect to its ability to make good on GenCo payments.

This ismore pronounced, given its lack of a track record, coupled with the yet- to-stabilise position of the DisCos. Without doubt, failure of the NBET will have a severe impact on each segment of the value chain.

For instance given that energy payments due to the gassuppliers for thermal plants is passed-through the GenCo tariff, failure to receive such from NBET will hurt the gas suppliers. Thus, the NBET must be strong enough to hold the commercial pieces of the chain together and adequately cover required payments upon the occurrence of availability events.

Whilst the NBET has gone through a few rounds of capitalisation by the FGN to approximately US$500 million, this is still adjudged insufficient given the expected generation capacity anticipated post-PHCN privatisation, and coming on stream of the NIPPs and new IPPs.

Indeed, there have been debates about feasible approaches to address the required capitalisation, and provide comfort for lenders and sponsors.

A recurring theme amongst suggested approachesis the need for government to use the proceeds of the PHCN privatisation to either capitalise the NBET or guarantee PPA payments, thus providing comfort for capital-at-risk, at least for the "forerunner"players.

As stated earlier, thisshouldcreate a demonstration effect on the sector. Strategies for this capitalisation still appear to be fluid, other than part proceeds of the recent US$1billion Eurobond.

In complementing planned FGN efforts to help de-risk the sector, the World Bank has committed to extending the coverage of its International Development Association (IDA)Partial Risk Guarantees (PRGs) from the gas segment to the generation and distribution segments.

The GenCo PRG is meant to backstop PPA payments from the NBET, while the DisCo PRG is meant to cover regulatory-induced revenue shortfalls, in the event that the retail tariffs are not reviewed as required and/or subsidies are not paid.

As helpful as this is, it is not exhaustive because the PRG isnot a limitless bucket. Given the assigned country limits, much of the bolstering should come from the government.

Half full, half empty?

Whilst the sector in light of the several constraints and bottlenecks in the value chain highlighted so far could be viewed as half empty, we like to view it as half full, not failing to acknowledge the successes recordedso far.

As Transaction and Financial Advisors that have witnessed the gradual evolution of the sector, we are able to creatively find solutions within our improving operating and regulatory environment, and duly advise our clients.

For instance, the transmission constraint, a major bottleneck, could be circumvented through the embedded generation model which allows for direct power off-take by the DisCos for their franchise areas, thus bypassing the weak transmission grid at the national level.Although, this comes with attendant risks, they can be mitigated through the fine art of deal structuring.

[14] Right of Way (ROW) usually is a significant cost element for stretching Transmission infrastructure

[15] These include Capacity, Energy and Ancillary services payments

[16] On occurrence of availability events (as agreed by buyer and seller), the GenCo is still entitled to due payments

Structuring Sustainable Projects and Companies

The Transaction and Financial Advisor's role in this process will continue as a driver of capital raising and financial engineering processes to create optimal structures for the development of projects and companies within the sector to help bridge the gap of the unmet demand.The increased capacity and appetite of investors, instigated by reformsthus far, will also be deepened by additional gains in the appropriate mitigation/allocation of risks.

Investors/Project Sponsors are able to access knowledge capital by engagingcredible legal, financial and technicaladvisors early in the deal structuring process to promote cohesiveness of the various constructs required for projects in the sector as illustrated in the typical IPP structure(Figure 3).

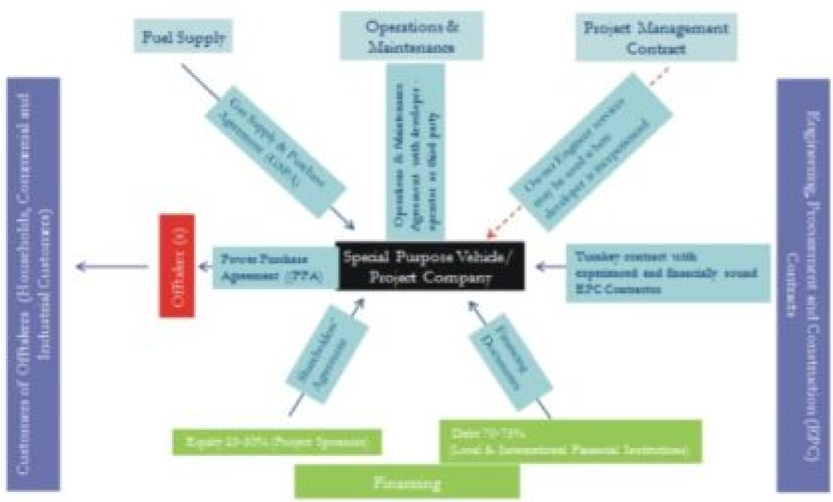

Figure 3: Typical IPP Transaction Structure and Contractual Framework

Managing the process to ensure that agreements between the various parties are binding, accrete favorable cash flows and appropriately allocate/mitigate risks is essential for the creation of value through deals. This is the role of the Advisors, bringing it all together through tested contracts and financial models for the analysis of investor prospects and decisions.

Evolving paradigms

The conclusion is that this is an evolutionary, not revolutionary, process. The one sure way to surmount the issues being faced is through experience. The more transactions the Advisor undertakes, the easier it is to replicate dexterous models for new projects. Over time, the Advisor will be able to build a robust information portal, Lenders will better realisethe low risk profile and steady cash flow potentials of projects in the power space, and the skills gap will be bridged as more people are exposed to power projects and transactions.

The Federal Government is on course in its bid to make the sector more attractive, as it debottlenecks the industry by investing in gas infrastructure, implementing the gas price per the agreed framework, and finalisingstandardised Gas Sale and Purchase Agreements ("GSPAs").

It is also mandatory for the Nigerian public to enter into a social contract with the process as a whole, and commit to cooperating to improve collections, stop electricity theft, pay agreed tariffs, etc. As concerns and issues are addressed, international players are also expected to become more active in the sector. The unifying goal is sustainable improvement in power generation and distribution systems translating into development of the economy, which we all can benefit from.

Gbenga has extensive private equity and corporate finance experience in the international and West African markets, spanning over 16 years. Gbenga has played a leading role in the origination and execution of power, gas and infrastructure deals at Àrgentil valued in excess of US$2bn. He also co-manages Àrgentil's principal investment activities.

He was previously with Aureos Capital where he originated and executed private equity transactions in Nigeria and Standard Bank / Stanbic Nigeria as Corporate Finance Manager.

He started his career with Syntegra, a Consultancy and Systems Integration business of British Telecom before moving to Standard Bank in London as a Manager of Finance Projects.

Gbenga holds a Bachelor's degree in Engineering and Business Management from the University of Greenwich, and a Masters degree in Economics and Management from the University College, London.
He is also a Chartered Certified Accountant in the UK (FCCA) and Nigeria (ACA).

NIPP AND THE GREAT NIGERIA POWER PRIVATISATION MOVING NIGERIA UP THE GLOBAL COMPETITIVENESS RANKINGS

Raj Kulasingam of Dentons UK

Here I am sitting (yet again!) at the airport, on my way back from Abuja. Purpose of visit - meet clients and attend the NIPP bidders conference. Most readers will be familiar with NIPP which I have touched on previously.

In broad terms, the Federal Government has launched a process to sell 80 per cent of its stake in ten companies (NIPP Gencos) that own gas-fired power plants that have been constructed or are in the late stages of construction to the private sector.

This is Part 2 of the Great Nigerian Power Privatization.

Moving forwards

Part 1 was the privatization of 15 generation and distribution companies which took place over the last two years. Reports indicate that 13 out of 15 of these companies have now been sold. With most of the new owners having paid the 75 per cent balance due to the government.

Full operational takeover of these companies is expected to happen soon and this should kick start the advent of the transitional electricity market in Nigeria.

In addition, successful bidders have been announced for the remaining two companies - Afam Genco and Kaduna Disco. One recent report announced that:

"Nigeria now stands on the verge of completing the largest electricity assets sale ever done in the history of the world."

On NIPP, it was recently announced that 82 consortia had been prequalified to bid for the sale of the 10 NIPP Gencos . Currently the NIPP Gencos are wholly owned by the Niger Delta Power Holding Company (NHPDC) which is running the tender process along with the Bureau of Public Enterprises (BPE). BPE and NHPDC are referred together in the rest of this article as the Government.

The sifting process

Although 82 consortia were pre-qualified, the following requirements should separate the wheat from the chaff [old English saying – also men from boys but I decided this was too gender specific!!!] whittle this number down over the coming weeks:

- Payment of $20,000 for the documents and access to the data room for each NIPP Genco [if 82 consortia paid this, that would be $1,640,000 – a good start to recouping the investment that has been made in constructing the plants?].
- Delivery of a US$4 Million on-demand payment bond. This is due on submission of bids which are currently due on 8 November 2013 [Although there were grumbles from a number of bidders for this deadline to be moved back during the bidders conference in Abuja. The messages from the Government were mixed with some saying that this was a line in the sand and there would always be some bidders asking for more time. However it seems that where we ended up was that the

Government would consider these requests for additional time.]

· Delivery of a bank guarantee equal to 15% of the amount bid by a bidder for the relevant NIPP Genco. This is to be delivered within fifteen (15) Business Days of official notification by the Government that a bidder has been made Preferred Bidder or Reserve Bidder. [A painful pill for the Reserve Bidder to swallow – not only coming second but also having to come up with this guarantee!! I suspect that most bidders would want to be either the Preferred Bidder or any other bidder but the Reserve Bidder. However, there could be instances when the Reserve Bidder could step into the shoes of the Preferred Bidder [E.g. the bids relating to Enugu and Sapele Disco in Part 1 – though I believe that this particular drama has not quite reached the end of the series!!]

· The bank guarantee can be called if a bidder fails to:

o accept the terms of any of the draft final Share Sale Agreement (SSA) or the draft final Shareholders' Agreement included in the bid documents [In response to a question on whether bidders were allowed to qualify their bid by marking up the documents, the response was no and bidders should price any such risks into their bid. This of course raises the question of what happens if an issue cannot be priced. For example if it goes to the bank ability of the transaction??]

o pay the required deposit upon signing of the Share Sale Agreement [the initial deposit is 25% of the purchase price for plants that are fully commercially available on the date of the SSA, and 10% of the Purchase Price for plants which are not fully commercially available on the date of the SSA.

The Bidders Conference

This was held in Abuja and was an opportunity for:

· the Government, its transaction advisers and other related parties to explain the structure of the projects, the key documents underlying the project , key issues and some timing and practical issues on the transaction; and

· bidders, advisers and suppliers to network and connect with a view to forming consortia and teams to bid for the NIPP Gencos.

The PPA and NBET – can they pay?

As is normal, the transactions have been structured with payments for power being made under a Power Purchase Agreement (PPA). The buyer of the power from the NIPP Genco will be a new company called the National Bulk Electricity Trader (NBET).

The key concerns for bidders on NBET is whether it is creditworthy enough to pay for :

· the monthly payments due to NIPP Gencos for generating power; and

· the termination payments that are due if the PPA is terminated.

The answer was that the Government was going to capitalise NBET adequately to cover its contingent liabilities. The issue that will be worrying bidders and lenders is how this money is going to be ring fenced to pay for these contingent liabilities and whether the amounts are enough to cover the monthly payments and termination payments.

Bidders were told that NDHPC had enough funds to fund 8 months worth of payments to the ten Gencos. The details around this, will be pored over by bidders and their funders in the coming weeks. Funders, being the conservative bunch they are, will probably require a great deal more financial cover and security over any monies that are allocated to pay for such claims.

There was also a discussion that the current structure of the NIPP was meant as an interim arrangement. That NBET would cease to exist once the recently privatized distribution companies were financially robust enough to covenant directly with the Generators. The mechanics of how this would happen and when was unclear – no doubt all will be revealed in due course but this is a critical bankability issue that will have to be overcome. Its likely that NBET will need to have some form credit enhancement for these projects to be bankable. Possible options are a Federal Government Guarantee, Partial Risk Guarantees, MIGA etc. The solution to this particular issue will have to be found over the coming weeks and is critical to the bankability of these projects.

Handover and condition of the plant

There was a lot of discussion about the condition of the plants that bidders will take over. Understandably the Government has taken the stance that the plants will be taken over on an "as is where is" basis. So bidders will have the opportunity to inspect the plants and the information in the data room and make their own assessment of the conditions of the plant and price their bids accordingly. This may be challenging for bidders bidding for plants that have not been commissioned and if time is not sufficient for bidders to made a proper assessment.

A related issue is the ability of an NIPP Genco to claim under the EPC Contracts for any defects in the plant. It did not seem clear if the original EPC Contract was entered into by the NIPP Genco or NDPHC. A point to consider when carrying out the due diligence is to review these EPC Contracts to understand what rights and obligations the Project Company has.

If the contracts were entered into by NDPHC, it would be normal to have the benefit of the rights (but not the obligations which should remain with NDPHC – technical legal point...) transferred to the Project Company. One for the due diligence team.

Gas Supply

The concerns on whether there will be gas to power these plants to their full capacity was also the subject of much discussion in Abuja. Gas supply infrastructure continues to be a key target for those seeking to attack foreign oil companies. One report stated that electricity generation in Nigeria has fallen 40% from its peak of 4,500 MW in December 2012 to 2,628 MW in August 2013. This was said to be largely attributable to interruptions in gas supply resulting from pipeline damage or sabotage.

Therefore, although NBET is taking fuel supply risk through the PPA [fuel supply failure is an Availability Event under the PPA], this "paper promise", together with concerns on NBET's creditworthiness could affect the bankability and pricing of the projects.

Evacuation

It is generally accepted that the transmission and distribution network has integrity issues affecting the adequate evacuation of the generated power. This was echoed in Abuja where the Transmission Company of Nigeria's (TCN) representative outlined plans to upgrade and develop the transmission network. It came across quite clearly that TCN did not currently have the requisite funds to be able to carry out all its plans.

In the context of NIPP, Capacity Payments under the PPA will continue to be made even if power cannot be evacuated as long as the plant is available. However the NBET covenant issue will continue to worry bidders in this context as well.

Funding

A key issue for the NIPP process is not only whether these projects are bankable but also whether banks will be willing to lend money to bidders wishing to buy them. Part 1 of the Great Nigeria Power Privatisation together with other projects like Dangote's refinery has sucked a lot of cash out of the Nigerian banking sector. Some say that this issue is further exacerbated by CBN restrictions on how much exposure a bank can have to any one sector such as the power sector. The development banks will not lend to these projects because there is no development element (e.g. the construction of the power plant). So will the international banks step in? Have they got the appetite for power projects in Nigeria?

Global Competitiveness – a footnote

Finally, the World Economic Forum last week released the Global Competitiveness Report 2013-14. Nigeria's ranking slipped to no 120 in the index of 148 countries from the previous year's position of no 115 (out of 144 countries). It stands at no 18 among African countries and sixth in West Africa. Respondents were also asked to name their five most problematic factors in doing business. Infrastructure and corruption lead with weighted shares of 23.5% and 21.3%. Sigh...... but perhaps the NIPP process will help move Nigeria's rankings north!

We all live in hope. Power to the people..... John Lennon and the Plastic Ono Band.

"This article was first published in the October 2013 edition of Financial Nigeria magazine."

Raj specialises in infrastructure and utility projects including projects in the power, transport (road and rail), water, waste and oil and gas sectors. He advises on concessions, the regulation of utility and transport companies and PFI/PPP projects. He has worked in the UK, the Middle East and Africa, acting for a mixture of developers, sponsors, lenders and governments.

He has been advising on PPP projects since the early 90s when the UK government initially started its PFI/PPP programme and advised on many ground-breaking PPP projects such as the Highways Agency's road PPP programme (including the multi billion pound M25 project), the MOD's water and wastewater project (Project Aquatrine), the first water treatment project in the UK (Project Alpha in Northern Ireland) and the first municipal PPP project in the Middle East (Ajman Wastewater).

A significant part of his practice has involved advising on projects in Sub-Saharan Africa. Projects he has been advised on include a police PPP project in Uganda, a hydro project in Zambia, rail and power projects in Nigeria, restructurings in Zimbabwe, private equity transactions in Nigeria and Ghana and oil and gas transactions in Nigeria

ACCESS TO NATURAL GAS: A glaring concern to development of IPPs

by John Delano of Akindelano Legal Practitioners (ALP)

If there is a concern for investors and proponents of the reformation of the Nigerian Power sector, it is the issue of adequate Gas supply. With the majority most of Nigeria's current power stations being Thermal, this issue is central to the success of the reform and has been the subject of debate for some time.

But the debate is fairly academic, especially when there are millions of borrowed dollars at stake. So in approaching the subject it is worth mentioning that Nigeria has one of the largest known reserves of natural Gas. There is, in fact, enough Gas to run the Power Sector, however 67% of local Gas produced (which is 4.4 bcfd) is exported.

In other words part of the problem is that until recently (due to the advent of Power reform), the domestic gas market has not lucrative enough to encourage local Gas companies to sell domestically. So like many thorny issues associated with the Nigerian space, this an issue of organisation poor management of resources and inadequate development of infrastructure. Nothing that is insurmountable for the forces of demand and supply.

For the sake of clarity I will re-state the problem by saying that Gas industry is plagued by 3 issues: 1) artificially low price of Gas, as a result of Government intervention . So far the government has only made small concessions on price. In the past, power stations paid as little as $1 per million British thermal units (Mbtu) for gas – a tiny fraction of US or European prices. Prices can now be as high as $2 or even $2.50 per Mbtu, but state regulators must still sign off on them first. 2) lack of investment in the infrastructure for transporting the Gas to the stations 3) inadequate number of players in the Gas space.

An historical perspective

Before the privatisation of Power sector, the erstwhile PCHN ambled along at a pace that suited its own peculiar nuances without any real attempt to secure long term Gas supply or raise the alarm about the need for investment in the Gas Sector. Indeed the amounts still owing by PHCN to a number of IOCs for Gas "purchased" is in the hundreds of billions. But live goes on, because there's no personal pinch to anyone's pockets. No real motivation for change.

The driver for any kind of activity and sustainable change in Nigeria is profit. In the past the absence of profitability has been at the heart of the dearth of interest and development in the Gas Sector. Indeed the only real progress in recent times has been the Gas Master plan drawn up by the government.

If you wish for the tidy organised perspective to the issue, get the Gas Master plan. It recognises the gap in infrastructure and is fairly comprehensive as an approach to the problem. But that is as far as it goes, and indeed as far as it can go. Where commerce is concerned, in the Nigerian context, nothing moves organically. Nigerians tend to react irrationally to issues facing them, however their reactions tend to be profound and dramatic. I daresay the picture we see today will change as the private sector players in both the Power and the Gas industries wake up to the real business of running power plants and begin to interact and form a formidable force to face up to the Governmental impediments.

So to put things in perspective, the problem has existed in abeyance for many years, but has only come to the fore because there is now a serious attempt to regenerate the Power industry. This in itself is a symptom that the problem is not an insurmountable one. It solutions rest on two things - the realisation of the Government that it is pursuing a counter- productive policy by keeping Gas prices artificially low; and the will of the Gencos and the Gas companies to make things work.

The effect of Privatisation

The recent privatisation and reform of the Power sector makes investment in Gas infrastructure more attractive and production for local consumption more lucrative. It is this potential for profit which has been lacking in the Gas industry.

This possibility of great gains will undoubtedly propel the industry forward to increase production and divert more supply for domestic use.

Gas companies are keener to deal with the new private sector owners of Gencos (than they have been with the Government owned national company) because the private sector has a much more positive payment culture. Indeed, the Gas Industry is starting to respond to the prospect of dealing with a more reliable clientele. Accordingly one of the new NIPP stations has managed to secured a Ten year agreement for the supply of Gas from Seven.

The price of Gas

However the price has to be right for this effect to follow so the Government will need to be convinced that a new era of privatisation necessitates a new approach the their pricing policy.

Potential solutions and positive developments Transportation infrastructure

There has been some progress on the transportation front. Seven Energy for instance has built several kilometres of pipeline to service Ibom Station. Also the likes of Oando and Nigerian Gas Company (part of NNPC) have announced their intention to build many Kilometres Gas pipeline which would support several Power stations. Medium term expansion prospects are good. In 2012 Shell announced 17 gas projects worth $6bn.

The Government has tried to address the issues in a number of ways - the most recent is the Emergency Gas plan launched in 2012 - run by the Government appointed Gas Aggregation Company of Nigeria (GACN). Other concrete initiatives include plans to build a petrochemicals plant by the Saudi firm Xenel industries, a fertiliser plant by India's Nagurjama, and a $3m gas plant for one of three CPF*s, by a consortium of Italy's Eni and local players Oando. (*central processing facilities).

Production Levels

With regard to production levels In 2011 production figures of usable Gas stood at 3.9 bcfd (according to BP figures). The 2011 total marks show an 11% rise on 2010 and there has been a 44% increase in the production of Gas in 2012.

The World Bank's efforts

In addition to the Government's efforts, the World Bank has set aside much need funds to guarantee the development of Gas infrastructure specifically to support the Power industry and the IPP model. See below details of the World Bank partial Risk Guarantee.

In April 22, 2013(Abuja) — The World Bank provided its first Partial Risk Guarantee (PRG) for US$145 million to support Nigeria's gas sector and bring more electricity to Nigerian consumers. The PRG agreements in support of a Gas Supply and Aggregation Agreement (GSAA) were signed today between the World Bank and the Power Holding Company of Nigeria (PHCN), Egbin Power PLC, Chevron Nigeria Ltd, and Deutsche Bank.

Under the 10-year GSAA, which is based on the industry template developed by Nigeria National Petroleum Corporation (NNPC), Chevron Nigeria Ltd will provide gas to Egbin power plant, thereby assuring gas availability and reliability for power generation and assisting in economic growth. This is the first time that Egbin power plant will be able to procure gas under long-term arrangements.

"With over 75% of Nigeria's power generation depending on natural gas, assuring the availability and reliability of gas supply is a critical step in realizing the goal of un-interrupted electricity supply to Nigerian consumers," said Marie Francoise Marie-Nelly, World Bank Country Director for Nigeria.

The World Bank PRG, provided under the IDA-financed Nigeria Electricity and Gas Improvement Project (NEGIP), was key to enabling long-term gas supply arrangements. PRGs are used to cover private lenders against the risk of a public entity failing to perform its payment or contractual obligations. The NEGIP PRG was instrumental in achieving financial closure of the Egbin GSAA transaction, by providing payment security for Chevron Nigeria Ltd for the supply of gas. The payment security instrument used was a 10-year Letter of Credit (L/C) issued by Deutsche Bank.

The absence of long-term gas supply arrangements has been one of the main causes of power shortages in Nigeria, as the gas had to be procured on a 'best endeavor' basis, which often was of low quality and insufficient quantity, resulting in poor performance of the power plants. The long-term contracts enabled by the PRG will also help encourage investments in upstream gas production by international and domestic oil and gas companies.

A race against time

All of the measures by the Government and the World Bank will go some way to easing the entry of new investors into the Gas Space and providing some succour for existing Gas companies as time goes on. However it will not affect the problem of Gas supply in the short term. It is very much a race against time, but even before the Gas issue, there will be the pressure to source for more funds to re-furbish their newly acquired Assets. This will create a lapse which give the Gas industry extra months to react. However that may be the new Gencos will be under pressure to forge alliances and relationships to alleviate their Gas needs sooner than later and the likelihood is that they will turn to the IOCs for a solution

Conclusion

The problem of access to Gas is not an insurmountable one. The new demand will force more Gas companies to enter the market. For now, the best hope for the supply of Gas are the major IOCs- they have both access to Gas and capability to put in place the pipeline transportation of the Gas. According to the NNPC, International Oil Companies account for 97% of total output, excluding flaring and reinjection. Shell is the clear leader -56% 2.22 mcfd; Agip is next 17%; Chevron 11% Total 9.1% Exxon Mobil. However the likes of Oando and NGC have also announced intentions to build new gas pipelines. But the most significant change required is the upward adjustment of price of Gas- it is the catalyst that will transform the Gas industry and put paid to all of the problems of production and transportation.

John graduated from Hull University with an LLB Honours decree in 1988. Thereafter he attended the Nigerian Law School and became registered Lawyer in Nigeria.

He practiced as a solicitor with Irving and Bonnar where he developed an interest in capital markets transactions, corporate restructuring and mergers and company law.

He followed this initial with a foray into the field of legal and corporate publishing working for reputable UK based companies like Kensington Publications, Informa and Tower Publishing, whilst acting as a consultant for ALP in the UK.

He has recently resumed full practice of Law in Nigeria actively pursuing strategic planning for ALP and her clients. He is keen to bring his UK experience to bear in the creation of journals for Oil and Gas, Logistics, Energy and Mining.

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